



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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Date: March 20, 2007

Contact Person:

Identification Number:

Contact Number:

EIN:

UIL: 511.00-00

Legend:

M =

N =

O =

Dear _____ :

This letter responds to your request for rulings under sections 501(c)(3) and 511-513 of the Internal Revenue Code.

Facts

You are a nonprofit corporation recognized as an organization described in section 501(c)(3) of the Code. Your stated exempt purposes are to promote _____ and to support, to the broadest extent possible, the _____ research program of M, a federal agency. In furtherance of this purpose, you engage in the following activities:

1. Operating _____ at M;
2. Managing fellowship and research grants that support programs at M; and
3. Administering group health insurance and other types of insurance programs for certain employees, contractors, and volunteers who work at or for M.

M operates trainee programs that provide an opportunity for recent pre-doctoral and doctoral degree recipients to pursue basic and _____ research at M facilities. M policy requires that trainees in these programs (collectively, "trainees") and others who work at or for M for at least 32 hours per week have adequate health insurance coverage. However, many trainees and other M workers are ineligible for federal health benefits because they do not qualify as government employees or are not present at M for 12 consecutive months.

Congress created N, a nonprofit organization separate and distinct from you, to help recruit and support researchers at M. An amendment to this legislation authorized N to administer M-related fellowships and grants that may include stipends, health insurance benefits, and other appropriate expenses. It also authorized N to use the resources of existing nonprofit

corporations with missions similar to that of N, including you, to provide these fellowships and grants.

You and N entered into an agreement, which is still in effect, under which you agreed to cooperate in providing services in support of M. Among other activities, you agreed to continue administering a group hospitalization and major medical plan for persons working at M who are not eligible for the health insurance plans available to federal employees. For many years prior to this agreement, you had administered a similar health insurance plan for M.

You have contracted with insurance company O to provide a basic group health insurance plan ("health insurance plan") that covers M trainees and other M workers who do not qualify for federal health insurance. These workers include guest researchers, exchange scientists, special volunteers, contractors, and full-time temporary employees. You negotiate the insurance contract with O, determine and process eligibility decisions, communicate the plan features and rates to subscribers, administer claims and billing issues, collect premiums, and monitor legislative developments that affect the health insurance plan. You represent that these are activities that would normally be carried on by an employer like M or other health plan sponsor, not by an insurance company or other third party payor.

M has adopted a written policy requiring that it pay for health insurance to cover trainees and their dependents. M pays the premiums for those trainees who elect to be covered under the health insurance plan to you, and you pay the premiums to O. If a trainee elects to obtain health insurance through another source, M will reimburse that trainee up to the premium amount that M would have paid if the trainee were covered under the health insurance plan. Almost all of M's workers who are covered under the health insurance plan are trainees, and almost all trainees are insured through the health insurance plan. The remaining trainees have other coverage via a spouse, sponsoring employer, or other source.

Although M could contract directly with O or another insurance company to provide basic health insurance to its workers who do not qualify for federal health insurance, M has chosen instead to contract

these responsibilities to you. M has done so to save money, maximize efficiency, and relieve itself of administrative burdens. You state that if M were to contract with O directly, each of M's centers for which its trainees work would have to obtain its own insurance contract with O, thereby increasing the overall administrative burden and cost to M. Separate contracts for each center would result in smaller pools of insureds and therefore higher premiums. Also, outsourcing its group insurance administrative responsibilities frees M from the related administrative burdens, freeing up resources to devote to its charitable and educational programs.

The contract between you and O requires you to make premium payments to O equal to the estimated claims for the following year. However, your potential liability under the contract is higher than the amount of your premium payments to O for that year. Accordingly, each year you collect from M a premium equal to the amount of your potential liability under the contract. You hold an amount equal to the difference between your premium payments to O and your potential liability under the contract in an internal reserve account to meet any future liabilities you may incur under the health insurance plan. If there is a surplus in the internal reserve account at the end of the year, after all claims are paid, then you retain such surplus and use it for other programs in furtherance of your exempt purposes, primarily in support of biomedical research activities at M.

In exchange for your administration of the health insurance plan, M also pays you an annual administrative fee.

Rulings Requested

1. Your administration of the health insurance plan lessens the burdens of government, and therefore your operation of the health insurance plan does not jeopardize your section 501(c)(3) tax-exempt status.
2. The income you receive from M related to administration of the health insurance plan is not subject to unrelated business income tax under the provisions of sections 511 through 513 of the Code.

Law

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax of organizations that are organized and operated exclusively for charitable, educational or scientific purposes, provided no part of their net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term “charitable,” as used in section 501(c)(3) of the Code, is to be construed in its generally accepted legal sense and may include lessening the burdens of government

Rev. Rul. 85-1, 1985-1 C.B. 177 provides that the determination of whether an activity lessens a burden of government is based upon (1) whether the organization’s activities are activities that a government unit considers to be its burdens, and (2) whether such activities actually lessen such governmental burden. An activity is a burden of government if there is an objective manifestation by the government unit that it considers the activities of the organization to be its burden. Such consideration may be evidenced by the interrelationship between the government unit and the organization. In this context, the lessening of the burdens of government is determined by considering all the relevant facts and circumstances. An organization’s performance of activities that a government unit treats as an integral part of its programs is evidence that the organization is lessening the burdens of government.

Rev. Rul. 85-2, 1985-1 C.B. 178 provides that the determination of whether an activity lessens a burden of government is based upon 1) whether the organization’s activities are activities that a government unit considers to be its burdens, and (2) whether such activities actually lessen such governmental burden. An activity is a burden of government if there is an objective manifestation by the government unit that it considers the activities of the organization to be its burden. A favorable working relationship between the government and the organization is strong evidence that the organization is lessening the burdens of government.

Section 511(a) of the Code imposes a tax on the unrelated business income of organizations described in section 501(c)(3).

Section 512(a)(1) of the Code defines unrelated trade or business taxable income as the gross income derived by any organization from any unrelated trade or business regularly carried on by it, less the allowable deductions directly attributable to such business activity, with certain modifications.

Section 513(a) of the Code defines unrelated trade or business as any trade or business the conduct of which is not substantially related (aside from the organization's need for funds or the use it makes of the profits derived) to the exercise of the organization's exempt purposes.

Analysis

Administering health insurance for trainees and others who work at M, but who do not qualify for health insurance benefits currently available to federal employees, furthers the exempt purpose of lessening the burdens of government pursuant to the criteria set forth in Rev. Ruls. 85-1 and 85-2, *supra*.

First, M considers this activity to be its burden. Promoting public health and supporting medical research are well established functions of state and local governments. In carrying out these functions, M seeks to attract and support research personnel by providing them with health insurance coverage. It does so, in part, through the health insurance plan, which is operated pursuant to specific legislative authority. Thus, administration of the health insurance plan is necessary to M's performance of its governmental responsibilities.

Furthermore, M has established a policy requiring that it pay for the health insurance of its trainees and their dependents. Under this policy, M transfers to you funds to cover premiums for trainees who elect coverage under the health insurance plan, and reimburses trainees who elect other coverage up to the health insurance plan's premium amount. M also pays you an administrative fee. By taking on financial responsibility for administration of the health insurance plan, M has further manifested its intent that the provision of health insurance is part of its burden.

Second, M's burden is actually lessened by your administration of the health insurance plan. The administration of this plan is an integral part of M's operations. Instead of administering the plan itself, M has contracted

with you to do so.

Your administration of the plan saves M money and ensures maximum efficiency by reducing the premium amounts that M pays for the insurance. Moreover, if M were to contract with O directly, each of M's centers would have to obtain their own insurance contracts with O, thereby increasing the overall administrative burden and cost to M. Thus, you are lessening the burdens of government by administering the health insurance plan.

Further, there is a close working relationship between you and M. M refers its workers needing health insurance to you to obtain coverage. You have administered group health insurance plans for M employees, contractors, and volunteers for many years. This close working relationship is further evidence that you are lessening the burdens of government according to the criteria set forth in Rev. Ruls. 85-1 and 85-2, *supra*.

Because your administration of the health insurance plan lessens the burdens of government, it qualifies as a "charitable" activity under section 501(c)(3) of the Code and section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations. Therefore, your administration of the health insurance plan does not jeopardize your section 501(c)(3) tax-exempt status.

Similarly, your administration of the health insurance plan is substantially related to your tax-exempt purposes, for purposes of section 513(a) of the Code, and the income you receive from M (*i.e.*, administrative fees and internal reserve account surplus) related to your administration of the health insurance plan is not unrelated trade or business taxable income under section

512(a)(1). Therefore, income you receive from your administration of the health insurance plan does not result in unrelated business income tax under section 511.

Rulings

1. Your administration of the health insurance plan lessens the burdens of government, and therefore your operation of the health insurance plan does not jeopardize your section 501(c)(3) tax-exempt status.
2. The income you receive from M related to administration of the health insurance plan is not subject to unrelated business income tax under the provisions of sections 511 through 513 of the Code.

This ruling is based on the understanding that there will be no material change in the facts upon which it is based. Any changes that may have a bearing on your tax status should be reported to the Service.

This ruling does not address the applicability of any section of the Code or regulations to the facts submitted other than with respect to the sections described.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Steven Grodnitzky
Manager
Exempt Organizations,
Technical Group 1

Enclosure: Notice 437

cc: